
PROPOSED BUDGET FINANCIAL SUMMARY

Financial Summary

General Fund Revenue

General Fund Revenue

Total General Fund revenue for the Fiscal Year 2005 Proposed Budget, including carryover from Fiscal Year 2004, is \$814.4 million, a 9.6 percent increase over the Annual Fiscal Year 2004 Budget. General Fund revenue funds core City services including police, fire, refuse collection, library services and parks and recreation programs.

Five major General Fund revenue sources – Property Tax, Sales Tax, Transient Occupancy Tax (TOT), Motor Vehicle License Fees (VLF), and Franchise Fees – comprise 67.1 percent, or \$546.1 million, of the City’s General Fund. These major revenue sources, as well as several other General Fund revenue sources, are highly sensitive to State and local economic conditions. Accordingly, this section largely focuses on the economic conditions that are relevant to each of the major General Fund revenue sources. In addition, this section discusses General Fund revenue sources that are less affected by economic conditions, such as Licenses and Permits, Fines, Forfeitures and Penalties, and Revenue From Other Agencies.

As the City approaches Fiscal Year 2005, economic conditions at all levels are improving. On the national level, Gross Domestic Product (GDP), the broadest measure of the economy’s health, has made substantial gains in the past six months, growing 4.1 percent in the fourth quarter of 2003, following a dramatic 8.2 percent gain in the third quarter. The third quarter’s growth in GDP marks the highest quarterly gain in nearly 20 years, while the previous two quarters combined represent the fastest back-to-back quarterly growth since the first two quarters of 1984. For all of 2003, GDP rose 3.1 percent, following 2.2 percent growth in 2002 and 0.5 percent growth in 2001.

After months of anticipation, the national job market appears to be finally setting a course for sustained growth. The Labor Department reported that non-farm payrolls grew by 308,000 in March 2004, the largest monthly gain since April 2000. March’s gain follows revised non-farm payroll growth of 46,000 in February and 159,000 in January. While the economy has seen positive monthly job growth since September 2003, the gains have routinely fallen short of economists’ predictions. According to non-farm payroll data from the Bureau of Labor Statistics, monthly job growth between September 2003 and February 2004 averaged just over 75,000, well short of the estimated 150,000 jobs per month needed just to keep pace with the labor force. Economists predict that job growth will have to average 200,000 per month to reclaim the more than 2.3 million jobs that have been lost since 2001.

Economic conditions are less positive at the State level, though continuing to improve. In March 2004, non-farm payroll employment in California rose by just 5,200 from the previous month, and 55,500 from March 2003. While California’s job gains in March represent just 1.7 percent of total nation-wide job gains, they represent the third straight month in which the California economy has added jobs on a year-over-year basis, after a full year of declines. The State’s unemployment rate increased to 6.5 percent in March, increasing from the revised 6.3 percent in February, but down from the 6.8 percent in March 2003.

Property Tax

Other Local Tax

- Sales Tax
- Safety Sales Tax
- Transient Occupancy Tax
- Property Transfer Tax

Licenses and Permits

Fines, Forfeitures, and Penalties

Revenue from Money and Property

- Interest Earning
- Franchise Fees
- Rents and Concessions

Revenue from Other Agencies

- Motor Vehicle License Fees
- Other

Charges for Current Services

Financial Summary

General Fund Revenue

The real estate market remains strong, with both median home prices and number of home sales setting records. According to the California Association of Realtors, the median price of a resale home reached \$468,450 in January 2004, a 20.7 percent increase over January 2003. Closed escrow sales of existing, single-family detached homes totaled 615,660 in January, at a seasonally-adjusted annual rate, the highest level on record. January's mark was 5.3 percent higher than the 584,600 sales pace recorded in January 2003.

As in the past, one of the largest challenges for California's economy will be the State's budget deficit, which the nonpartisan Legislative Analyst Office (LAO) estimates to be approximately \$17 billion, which reflects an estimated deficit of a \$15 billion for the 2004-05 Fiscal Year, and a \$2 billion shortfall in the current fiscal year. A partial solution to this shortfall, as outlined in the Governor's Fiscal Year 2005 State Budget Proposal, is a one-time issuance of up to \$15 billion in Economic Recovery Bonds, which was recently approved in the March 2, 2004 statewide election. However, even if the Governor's Budget Proposal is passed in its entirety, the LAO estimates that the State will still be facing an \$800 million deficit in Fiscal Year 2005, as well as an ongoing structural deficit of nearly \$7 billion that would exist beyond the budget year, absent any corrective action.

Locally, San Diego's economy continues to outperform both the State and national economies. The San Diego Regional Chamber of Commerce Economic Research Bureau estimates that the Gross Regional Product (GRP) in 2003 was a record \$129.2 billion, a 5.5 percent increase over the 2002 estimate. The Chamber is forecasting even stronger growth in 2004, projecting a 6.2 percent increase in the GRP to \$137.2 billion. In February, San Diego County's unemployment rate fell to 3.9 percent on an unadjusted basis, down from a revised 4.1 percent in January and 4.4 percent in February 2003. Positive indicators for the San Diego region are the housing market, which has seen continual increases in both median price and number of sales, and the tourism market, which set a record in 2003 with 26.4 million people visiting the region. These and other local factors are discussed in greater detail throughout this section.

Property Tax

The City of San Diego receives Property Tax revenue based upon a one percent levy on the assessed value of all real property. Property tax revenue is collected by the County of San Diego, which allocates the revenue to a number of agencies within the City's geographic area, including the County itself, the City of San Diego, school districts, and special districts.

Prior to 1979, each local jurisdiction had the authority to levy its own property tax. Thus, a single residence might have been subject to a separate tax levy by the City, the County, the school district, and any special districts that served the residence. In 1979, California voters passed Proposition 13, dramatically changing the face of State and local public finance. Proposition 13 limited the aggregate property tax rate to one percent of assessed value, and specifies that the assessed value of any real property may increase by a maximum of two percent per year based on the 1976 value, unless the property is improved or sold at which time the property is reassessed at market value. Under the current system established by Proposition 13, all local jurisdictions receive a share of the one percent tax levy. For every \$100 collected, the City of San Diego receives approximately \$16.90.

**Total City Budget
\$224.7 million**

**General Fund
Budget
\$216.0 million**

**Percent of
General Fund
26.5%**

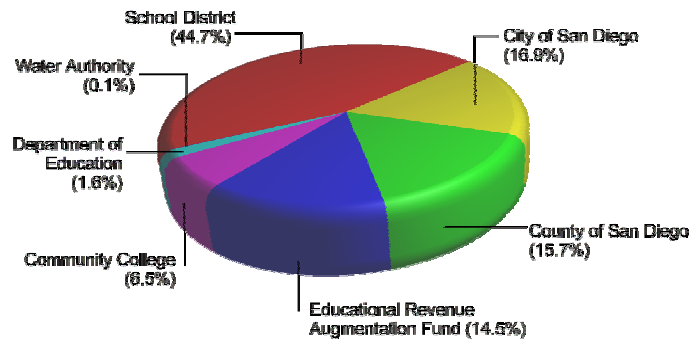
Over the past decade, many factors have contributed to reductions in the amount of Property Tax revenue the City has received. In Fiscal Years 1993 and 1994, the State took action to reduce its obligation for school funding by shifting local Property Tax revenue to school districts, in what is now referred to as the Educational Revenue Augmentation Fund (ERAF) shifts. This reallocation of funds caused a permanent

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General Fund Revenue

shift in City Property Tax that will result in a cumulative loss of over \$341 million through Fiscal Year 2004. In addition, the State authorized counties to charge administrative fees to cities for collecting and distributing Property Tax. For the City of San Diego, that action has further reduced annual Property Tax receipts by approximately \$2.1 million per fiscal year. In addition, increasing property values in Redevelopment Areas does not increase the General Fund share of Property Tax revenue, as any increase in Property Tax due to redevelopment must stay in the Redevelopment zone.

PROPERTY TAX ALLOCATION



In Fiscal Year 2005, the City's Property Tax revenue is once again in jeopardy of being confiscated by the State. The Governor's Proposed Fiscal Year 2005 State Budget, presented on January 9, 2004, proposes to shift \$1.3 billion in Property Tax revenues from local governments (including redevelopment agencies) to school districts. This ERAF shift, if implemented, could result in the loss of as much as \$9.5 million from the City's General Fund. This potential revenue loss has not been incorporated into the City's Fiscal Year 2005 Proposed Budget, since no decisions about the State budget were final at the time the City's budget was developed.

The Fiscal Year 2005 Proposed Budget for Property Tax is estimated at \$216.0 million, an eight percent growth over Fiscal Year 2004 year-end projections. This projection reflects a real estate market that remains strong, and is showing no indication of an immediate slowdown. According to DataQuick, a local housing industry research company, the median price of an existing detached single-family home in San Diego County in March was \$456,000, a 22.6 percent increase over the median price in March 2003, and \$14,000 higher than in February 2004. Since January 2003, the median price has increased \$31,000, the highest two-month price gain on record for single-family resale homes. The median price for all home sales (including condominiums and condo conversions) reached a record \$424,000 in March, up nearly 17 percent from the previous year and surpassing the previous record of \$406,000 set in February. On the statewide level, the California Association of Realtors reports that sales of existing detached single-family homes in calendar year 2003 have exceeded 2002's record setting pace of 572,500 units.

The City's Property Tax revenue has experienced strong growth over the past five fiscal years. Between Fiscal Years 1999 and 2004, Property Tax revenue has averaged 8.9 percent annual growth, compared to the previous decade, where Property Tax growth averaged just 1.2 percent per year between Fiscal Years 1990 and 1999. Much of the low growth during the 1990s was due to sizeable Property Tax shifts to ERAF in 1993 and 1994. Even adjusting for these shifts, average growth between Fiscal Years 1990 and 1999 was just 3.4 percent.

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General Fund Revenue

Property Tax revenue is expected to maintain strong growth for the next several fiscal years, although slowing from the peak of 10.43 percent in Fiscal Year 2000. Record-low mortgage rates have fueled much of the appreciation in housing prices, as prices rise commensurately with purchasing power. In addition, the City's population growth and lack of land available for residential development have resulted in an imbalance between the supply of and demand for homes. The major risk to Property Tax revenues in the next few years is inflation. According to the UCLA Anderson Forecast, a sudden increase in inflation will cause mortgage rates to rise significantly, and the housing market to quickly slowdown. Anderson does not expect any significant increases in inflation, and they are projecting a slow increase in mortgage rates over the next two years.

Property Tax is also collected for purposes other than supporting the General Fund. As allowed by Proposition 13, an additional levy above the one percent rate is collected to pay for debt service on voter approved debt. In June 1990, voters approved a \$25.5 million debt issuance to finance a public safety communication system for the City. With a current balance of \$14.4 million, the levy was \$1.80 per \$100,000 of assessed valuation in Fiscal Year 2004. The Fiscal Year 2005 rate is to be determined later in the current year with the Tax Rate Ordinance. In addition, a special tax levy of \$5.00 per \$100,000 assessed valuation is used to fund zoological exhibits.

Other Local Taxes

Sales Tax

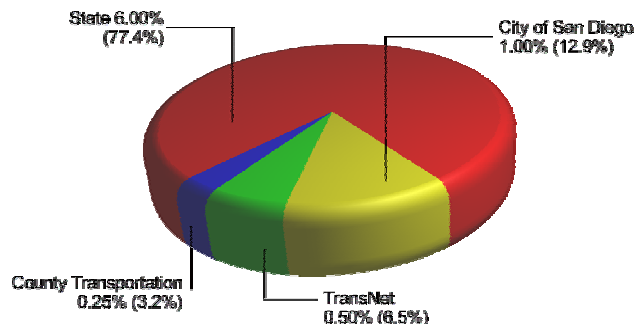
Sales Tax is the City's second largest source of revenue in the General Fund. Collected at the point of sale, Sales Tax revenue is remitted to the State Board of Equalization, which allocates tax receipts owed to the City in the form of monthly payments. The City receives one cent (or 13.0 percent) of the total 7.25 cent statewide Sales Tax levied on each dollar of taxable sales. In addition, San Diego County voters approved a half-cent supplemental Sales Tax in 1987 to fund the San Diego Transportation Improvement Program (TransNet), resulting in a total Countywide Sales Tax of 7.75 percent.

Total City Budget
\$202.7 million

General Fund Budget
\$132.6 million

Percent of General Fund
16.3%

SALES TAX ALLOCATION



The Fiscal Year 2005 Proposed General Fund Budget for Sales Tax revenue is estimated at \$132.6 million, a 3.5 percent growth over Fiscal Year 2004 year-end projections. This conservative projection is reflecting stronger growth in the San Diego economy, while taking into account some of the risks facing Sales Tax growth, such as rising consumer debt and gas prices, and the proliferation of variable interest

Financial Summary

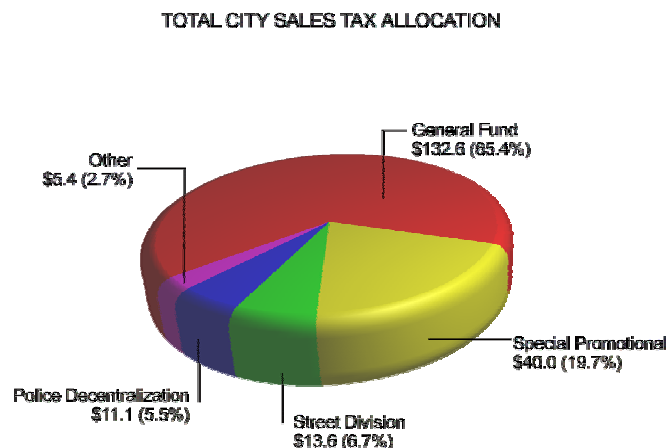
General Fund Revenue

rate mortgages. As interest rates increase, consumers holding variable-interest debt will have less income with which to generate taxable sales.

Sales Tax revenue is highly sensitive to economic conditions, and reflects the levels of unemployment, consumer confidence, per-capita income, and business investment. These factors have a positive relationship with taxable sales, which is the main determinant of Sales Tax revenue. San Diego County added 6,700 jobs in the third quarter of 2003, after losing jobs in the first and second quarters. According to the State's Employment Development Department, total wage and salary employment in San Diego County averaged 1,418,300 in 2003, a 1.7 percent increase over the 2002 average. The County's unemployment rate fell to 3.9 percent in February, down from 4.1 percent in January and 4.4 percent in February 2003. Total wage and salary employment increased by 7,600 in February, giving San Diego the fourth lowest unemployment rate in the State behind only Marin, Orange and San Luis Obispo Counties. The drop in San Diego's unemployment rate came with an increase in the labor force, indicating that the region's labor market is poised to handle the growth in population.

Nationally, same-store retail sales, defined as sales at stores that have been open for at least one year, grew by 4 percent in December, making the 2003 holiday the strongest shopping season in four years, according to the Goldman Sachs index of same-store sales. In March 2004, retail sales rose 1.8 percent, the largest monthly gain in retail sales since March 2000 and three times greater than Wall Street analysts had projected. Although there are no solid figures for consumer spending at the local level, San Diego's retail sales probably grew at a faster pace than the nation as a whole, according to the San Diego Regional Chamber of Commerce, Economic Research Bureau.

Business fixed investment, the primary engine behind the boom of the late 1990s and the main cause of the recession in 2001, is recovering solidly. The Commerce Department reported that non-residential business spending increased 9.6 percent in the third quarter of 2003, following a 12.8 percent growth in the third quarter. Growth in the third quarter represented the fastest rate since early 2000. Meanwhile, corporate profits increased 7.2 percent in the fourth quarter 2003, following a 9.9 percent and 10.3 percent growth in the third and second quarters, respectively.



As with Property Tax, Sales Tax is in danger of being diverted by the State of California. On March 2, 2004, California voters passed Proposition 57, The Economic Recovery Bond Act. The passage of this Proposition will result in the one-time issuance of an Economic Recovery Bond of up to \$15 billion to

Financial Summary

General Fund Revenue

pay off the accumulated deficit in the State's General Fund. The financing of this bond will be done through a complex revenue shift, by which local governments will lose $\frac{1}{4}$ -cent of their Bradley-Burns Sales and Use Tax. This revenue shift, commonly known as the "triple-flip," then stipulates that the $\frac{1}{4}$ -cent will be re-enacted at the State level and used as a dedicated revenue source to finance the Economic Recovery Bond. In an effort to hold local governments harmless, Property Tax will be shifted from school districts in an equivalent amount to the Sales Tax that is lost. However, due to the mechanics of this shift, growth on the shifted Property Tax revenue will not be realized until the following year from when the growth actually occurs. In other words, local government will not receive Fiscal Year 2005 growth on the shifted revenue until Fiscal Year 2006. For the City of San Diego, this is projected to result in \$1.7 million in shifted Property Tax revenue that will not be received until Fiscal Year 2006. This triple-flip has been incorporated into the Sales Tax projections for Fiscal Year 2005.

Safety Sales Tax

Safety Sales Tax revenue is derived from a half-cent Sales Tax, approved by voters on November 2, 1993 with the passage of Proposition 172, which must be utilized solely for local public safety purposes. The State Controller's Office disburses Safety Sales Tax revenue to the County Local Public Safety Fund for distribution. Cities receive five percent of the amount in the Fund based upon their 1993-94 allocation that was derived from their proportionate loss of Property Tax revenue to school districts. Subsequent legislation (Senate Bill 8) changed the allocation system for Proposition 172 revenue and lifted the cap on the share that the City of San Diego and other cities within the County could receive. Total revenues reflect additional funds received by the City as a result of this legislation.

**Total City Budget
\$6.7 million**

**General Fund
Budget
\$3.9 million**

**Percent of
General Fund
0.5%**

The Fiscal Year 2005 Proposed Budget projects Safety Sales Tax at \$6.7 million, a three percent growth over Fiscal Year 2004 year-end estimates. Approximately \$2.8 million in Safety Sales Tax revenue is allocated for debt service payments on Fire and Lifeguard Facility improvements. The remainder, or approximately \$3.9 million, is allocated for public safety expenditures within the General Fund. City Council Policy 500-07 directs the use of Proposition 172 funds for new public safety expenditures to ensure an augmentation of existing General Fund public safety expenditure levels. Increases to public safety expenditures in the Police and San Diego Fire-Rescue departments have far exceeded the revenue growth of Safety Sales Tax, ensuring the City's compliance with Council Policy 500-07. Further discussion of public safety expenditures can be found in the section on public safety.

As with regular Sales Tax revenue, Safety Sales Tax revenue is sensitive to economic conditions, particularly factors that influence taxable sales, such as employment levels, consumer confidence, per-capita income, and business investment. However, Safety Sales Tax is allocated to counties in proportion to their share of taxable sales, and as a result, the City's share of total County-wide Safety Sales Tax revenue depends not on taxable sales within the City, but rather on the County's share of total statewide taxable sales.

Financial Summary

General Fund Revenue

Transient Occupancy Tax

Transient Occupancy Tax (TOT) is levied on the daily rental price for rooms in hotels and motels used by visitors staying in San Diego for less than one month. The hotel tax or room tax, San Diego's TOT is levied at ten and one-half cents per dollar of the daily room price. Currently, an equivalent of five cents of the TOT, approximately 48 percent, is allocated to Special Promotional Programs for the promotion of tourism and other purposes designated by City Council policy. The remaining five and one-half cents, approximately 52 percent, is allocated directly to the General Fund for general government purposes. The TOT was last raised in August 1994, when the rate was increased by one and one-half cents per dollar.

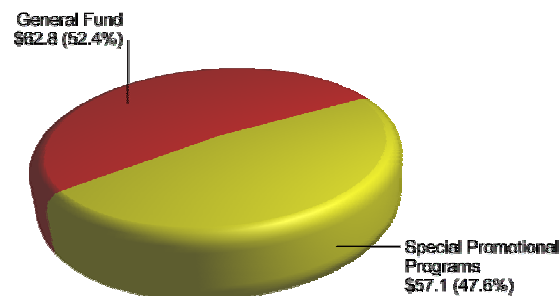
Total City Budget
\$119.9 million

General Fund Budget
\$62.8 million

Percent of General Fund
7.7%

The Fiscal Year 2005 Proposed General Fund Budget for TOT revenue is estimated at \$62.8 million, reflecting continued strong performance by San Diego's tourism industry. The Fiscal Year 2005 projection assumes a six percent growth over Fiscal Year 2004 year-end estimates, adjusted for estimated TOT revenue from new hotels associated with the new Ballpark.

TOTAL CITY TRANSIENT OCCUPANCY TAX ALLOCATION
(In Millions)



San Diego continues to be among the top travel destinations in the country. Smith Travel Research reported that in the months of July and August in 2003, San Diego County's hotel occupancy rate was 85 percent and 84 percent respectively, the highest marks among the top 25 metropolitan markets. Through October, only the cities of New York, Oahu and San Diego had annual occupancy rates over 70 percent. Several factors have contributed to San Diego's comparative advantage over other travel destinations. According to a joint report from the San Diego Convention and Visitors Bureau (ConVis) and the Center for Hospitality and Tourism Research at San Diego State University, approximately two-thirds of all visitors to San Diego County come from other parts of California and Arizona, making San Diego primarily a "drive-in" market, and hence less affected by the decline in airline travel. In addition, the report stated, travel patterns have shifted in the last few years to reflect a preference for shorter, closer-to-home types of vacations – a good match for San Diego's perception as "a little paradise, not too far away."

The main challenges facing San Diego's lodging industry have been the decline in business international travel. Business travel has declined over the past several years as corporations have cut back on spending, although increased business travel was evident in the third and fourth quarters of 2003. According to the San Diego Convention & Visitors Bureau, San Diego has done well with meetings and conventions, but individual business travel continues to struggle, whether because of tighter budgets,

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General Fund Revenue

safety concerns, or some other reason. International travel continues to be a struggle as well. The San Diego State University's Center for Hospitality & Tourism Research attributes the decline in international travel to a lingering effect of the terrorist attacks on September 11, 2001. Homeland Security measures and new rules forcing tourists to get visas or travel documents before they leave their home country have made international travel more difficult.

On March 2, 2004, a proposal to increase the City's TOT rate failed to win the necessary 2/3 approval by San Diego voters. The proposal would have increased the TOT rate to 13 percent.

Property Transfer Tax

A Property Transfer Tax is levied on the sale of real estate property. The County charges \$1.10 per \$1,000 of sale price when any real property is transferred. The City of San Diego charges \$0.55 per \$1,000, which is credited against the County's charge, so that the City and the County both receive \$0.55 per \$1,000. The funds are collected by the County Recorder for property transfers that occur within City limits, and transferred to the City in 13 apportionments throughout the year.

The Fiscal Year 2005 Proposed Budget projects Property Transfer Tax revenue to be \$10.6 million, a six percent growth in Property Transfer Tax revenue, reflecting strong sales of residential and commercial property. Record-low mortgage and bank loan rates have fueled investment in residential and commercial real estate. While the residential market is contributing to healthy property transfer tax revenue by setting records for sales and price appreciation, the commercial market is also doing well. According to Burnham Real Estate Services, investors purchased more than \$4.2 billion of commercial real estate in 2003. Office sales alone have accounted for approximately \$1.3 billion, an increase from \$999 million in 2002. According to brokers from Burnham, San Diego County's real estate market is expected to remain at least as strong in 2004.

While commercial real estate sales are fewer in number than residential sales, each transaction generates a greater amount of property transfer tax. Noticeable commercial sales in 2003 include Symphony Towers at \$134 million, the First National Bank Center at \$112 million, and the Promenade Rio Vista Phase I in Mission Valley, at \$101.5 million.

Total City Budget
\$10.6 million

General Fund
Budget
\$10.6 million

Percent of
General Fund
1.3%

Licenses and Permits

The Licenses and Permits category reflects revenue generated to recover costs associated with performing regulatory functions. These functions are typically performed by government due to public safety considerations. The Fiscal Year 2005 Proposed General Fund Budget for Licenses and Permits is estimated at \$22.3 million, a 4.7 percent decrease over the Annual Fiscal Year 2004 Budget. Major budgeted revenues in this category include general business license taxes, rental unit taxes, parking meter collections, and the refuse collector business license tax.

The general business license tax for companies with 12 or fewer employees is a flat rate of \$34. Companies with 13 or more employees pay a flat fee of \$125 plus \$5 per employee. Rental unit taxes are calculated as a flat rate plus a fee per rental unit. Currently, the rental unit tax has three rate tiers for residential properties and two rate tiers for hotel/motel properties.

Total City Budget
\$54.9 million

General Fund
Budget
\$22.3 million

Percent of
General Fund
2.7%

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General Fund Revenue

Fines, Forfeitures, and Penalties

Fines, Forfeitures, and Penalties include revenue generated from monetary sanctions associated with the violation of a law or regulation such as California Vehicle Code violations, City parking and ordinance violations, and litigation awards. The Fiscal Year 2005 Proposed General Fund Budget for Fines, Forfeitures, and Penalties is estimated at \$30.3 million, a 3.0 percent increase over the Annual Fiscal Year 2004 Budget.

Total City Budget
\$31.4 million

General Fund Budget
\$30.3 million

Percent of General Fund
3.7%

Revenue from Money and Property

Franchise Fees

Franchise Fees are paid to the City of San Diego by private utility companies in exchange for the permission to use the City's rights-of-way. Franchise Fees are usually charged as a percentage of gross sales, although other types of charges are common. Rates are set through Franchise Agreements that are negotiated with individual utility companies, which often contain provisions for renegotiation after a standard period of time. The City of San Diego currently has franchise agreements with San Diego Gas & Electric (SDG&E), Cox Communications, and Time Warner Cable. In addition, the City collects a Refuse Haulers Franchise Fee from private refuse haulers.

Total City Budget
\$106.8 million

General Fund Budget
\$56.8 million

Percent of General Fund
7.0%

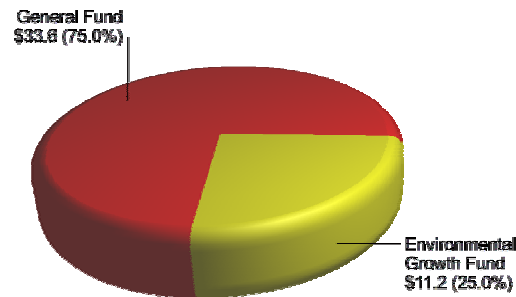
The Fiscal Year 2005 Proposed Budget projects General Fund Franchise Fees to be \$56.8 million. This projection assumes a five percent increase in gross sales over year-end estimates for SDG&E, Cox Communication, and Time Warner, while Refuse Hauler Franchise Fees are projected to increase 20 percent over year-end estimates. The Fiscal Year 2005 Proposed Budget projection also includes the annualization of the Time Warner rate increase from three percent to five percent that became effective on January 8, 2004. The Franchise Agreement with Cox Communications was renegotiated in 2002, which increased the Franchise Fee charged to the cable provider from three to five percent of gross sales. In addition, the Refuse Hauler Franchise Fee was increased by \$1 in July 2003 to an effective rate of \$11 per ton for Class I haulers (less than 75,000 tons per year) and \$12 per ton for Class II haulers (more than 75,000 tons per year).

SDG&E, the single largest generator of Franchise Fee revenue, is charged three percent of gross sales from gas and electricity within the City of San Diego. Three-fourths of total SDG&E Franchise revenue is allocated to the General Fund, while one-fourth is required to be allocated to the Environmental Growth Fund (EGF). One-third of the SDG&E revenue in the EGF is used to finance various environmental programs such as regional park and open space maintenance; two-thirds is used for debt service on open space acquisition bonds.

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TOTAL CITY SDG&E FRANCHISE FEE ALLOCATION
(In Millions)



In addition to the current three percent Franchise Fee, the City Council approved a 3.53 percent surcharge on electricity sales for the undergrounding of electric utility lines. The surcharge is estimated to raise \$38.8 million per year for the City, to be used solely for the purpose of placing utility lines underground. The surcharge was approved by the California Public Utilities Commission in December 2002. This revenue is deposited into a separate fund.

Franchise revenue from SDG&E remains unstable. Late in the year 2000, an unusual spike in natural gas prices sent utility bills soaring. As a result Franchise revenue from SDG&E increased by nearly 45 percent in Fiscal Year 2002. However, the unusually high natural gas prices did not last, and in Fiscal Year 2003, SDG&E Franchise revenue fell almost 33 percent. Even though SDG&E Franchise revenues are projected to finish Fiscal Year 2004 with a 21 percent gain, the average growth over the last five years has been under 10 percent. Due to the instability over the past several years, the City has set a more conservative estimate.

Interest Earnings

The City Treasurer is responsible for investing the City's cash assets exclusive of City Pension Trust Funds. All City funds are pooled and invested together in a Pooled Investment Fund ("Fund") to facilitate increased flexibility in the management of the City's cash flow requirements and the overall management of the Fund for the purpose of maximizing interest earnings. Fund investments must be consistent with the City Treasurer's Investment Policy and the State of California Government Code guidelines and restrictions. The maximum maturity of any investments may not exceed five years. Selection of an investment is based on safety, liquidity, risk, interest rate environment and the cash flow requirements of the City. Major deviations in returns from one fiscal year to the next can generally be attributed to changes in market interest rates or the actual average amount invested during the fiscal year. Past interest earnings performance is no guarantee or indicator of future results.

Total City Budget
\$17.5 million

General Fund Budget
\$1.2 million

Percent of General Fund
0.1%

Interest rates, which had been declining for a number of years, reached their lowest levels in June 2003 and have been rising since then. This change in the overall level of interest rates is reflected in the interest earnings for Fiscal Year 2004, which takes into account the realization of any gains or losses on portfolio securities which occur as securities are regularly turned over during the fiscal year. In a rising interest rate environment the value of securities held in the portfolio declines while the converse is true in

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a declining interest rate environment. When this change in portfolio value occurs, the impact on overall interest earnings, whether positive or negative, is mitigated to some degree by the earnings derived from the reinvestment of cash from the turnover of portfolio securities and the investment of new revenues at current market rates of interest.

Interest rates are expected to continue to rise through the remainder of Fiscal Year 2004 and most of Fiscal Year 2005. The adverse effect of rising interest rates on the value of the securities in the portfolio will be mitigated by the reinvestment of maturing and sold securities at higher interest rates, which will result in higher earnings in the future. It should be noted that interest rates continue to be volatile and subject to a number of uncontrollable or predictable factors.

Based on these factors, the Fiscal Year 2005 Proposed Budget projects Interest Earnings to be \$1.2 million, unchanged from Fiscal Year 2004.

Rents and Concessions

The Rents and Concessions category includes General Fund revenue generated from Mission Bay Park, Balboa Park and Torrey Pines Golf Course. The Fiscal Year 2005 Proposed Budget projects Rents and Concessions at \$32.7 million, a 4.2 percent growth over the Annual Fiscal Year 2004 Budget. The largest component of this category is Mission Bay Park rents and concessions revenue, the majority of which is generated from leases with Sea World, Marina Village Conference Center, and hotels and marinas within Mission Bay Park. This revenue source is projected at \$23 million in Fiscal Year 2005, with \$21.5 million being allocated to the General Fund. The Mission Bay Ordinance requires that one-half of all revenue from Mission Bay rents and concessions in excess of \$20 million is to be allocated to the Mission Bay Improvement Fund and the Regional Park Improvement Fund. The Mission Bay Improvement Fund is to be used only for permanent public capital improvements and deferred maintenance of existing facilities in Mission Bay pursuant to the Mission Bay Park Master Plan. The Regional Park Improvement Fund is to be used only for permanent public capital improvements, planning, deferred maintenance, and for land acquisition for San Diego Regional Parks. The Fiscal Year 2005 Proposed Budget estimates an allocation of \$750,000 to each of these funds.

Total City Budget
\$54.8 million

General Fund Budget
\$32.7 million

Percent of General Fund
4.0%

Another component of this category relates to revenue generated from lease agreements on City Pueblo lands, which in Fiscal Year 2005 is projected at \$3.1 million.

Revenue from Other Agencies

Motor Vehicle License Fees

Motor Vehicle License Fees (VLF) are levied as a percentage of an automobile's purchase price, subject to depreciation, and are paid annually to the Department of Motor Vehicles at the time of registration. The fees are forwarded to the State Controller's Office, which allocates the funds to local governments. Prior to Fiscal Year 2004, approximately 25 percent of total statewide VLF revenues were allocated to counties in order to fund realignment of various health and social service programs, while the remaining 75 percent was allocated to cities and counties on a per capita basis. Notably, because statewide revenues are distributed on a per capita basis, increases to local vehicle sales do not directly translate into local MVLF revenue increases.

Total City Budget
\$78.0 million

General Fund Budget
\$78.0 million

Percent of General Fund
9.6%

Financial Summary

General Fund Revenue

In 1999, the State legislature enacted a 67 percent offset in the MVLF, from two percent of a vehicle's value to 0.65 percent. To compensate cities and counties for the tax offset, the State has backfilled the loss of revenue to cities and counties from the State General Fund. However, a large budget deficit in Fiscal Year 2004 prompted Governor Davis to invoke the "insufficient moneys" clause (State Revenue & Taxation Code, Section 10754(a)(3)(A)), eliminating the 67 percent VLF offset, and with it, the backfill payments to local governments. The backfill was eliminated on June 19, 2003, while the rate increase did not take effect until October 1, resulting in a three month "gap" in VLF funds for local governments. However, counties could not afford to lose revenue that was allocated for program realignment, so for Fiscal Year 2004, the percentage of VLF dedicated to counties for realignment programs increased to 28 percent. As a result, local governments were hit twofold, first by the three month "gap" in funding, and second through a reduced percentage of the total statewide VLF allocation.

The Fiscal Year 2005 Proposed Budget for VLF is \$78.0 million, a three percent increase over Fiscal Year 2004 year-end projections, adjusted for the backfill revenue that was lost as a result of the gap. As part of the Fiscal Year 2005 Proposed State Budget, presented on January 9, 2004, the Governor proposed to restore VLF backfill funding to its full amount. Furthermore, state law stipulates that the percentage of total statewide VLF dedicated to counties for program realignment will revert back to its prior level. The City's Fiscal Year 2005 Proposed VLF budget projection takes both of these factors into account.

Nationwide auto sales in December 2003 came in at 18 million units on an adjusted annual basis according to AutoData, an automotive research firm. Monthly auto sales are commonly measured as an adjusted annual rate, meaning the number of sales that would occur in one year if the current monthly pace was maintained, adjusting for monthly variation. December's mark was below the 18.2 million-unit rate posted in December 2002, but was the second highest annual rate in 2003, behind only August's adjusted annual rate of 19 million vehicles. For the entire year, vehicle sales totaled just under 16.7 million units, a 1 percent decline from 2002, making 2003's total the lowest since 1998, though still the fifth best year on record.

Another challenge facing the automotive industry is pricing power, as consumers have become accustomed to low-interest financing and other deep incentives. According to Paul Taylor, chief economist with the National Automobile Dealers Association, automakers have begun raising prices on new car models, but then offsetting the increases with incentives. In 2004, they plan to ease back on incentives in the hopes that a wave of new models will entice consumers to continue purchasing vehicles.

Other

A significant amount of revenue received by the City is initially collected by other agencies and then returned (or subvended) to the City. Within the General Fund, Revenues from Other Agencies include federal and State grants, and reimbursement for general City services provided to the Unified Port District.

The Fiscal Year 2005 Proposed Budget includes revenue totaling approximately \$10.9 million in this category, including \$5.2 million in State reimbursements for booking-fee related expenses. However, the Governor has proposed eliminating booking fee reimbursements to cities. The City expects to receive \$2.5 million from the State for the Community Policing Services (COPS) Program and \$1.2 million in Local Law Enforcement Block Grant. The State Police Officer Standards and Training (POST) grant reimbursement, included in the General Fund beginning in Fiscal Year 1995, is budgeted at \$100,000.

**Total City Budget
\$121.8 million**

**General Fund
Budget
\$10.9 million**

**Percent of
General Fund
1.3%**

Financial Summary

General Fund Revenue

Charges for Current Services

Charges for Current Services includes revenue generated by General Fund departments resulting from services provided to other City funds. General Fund departments regularly incur expenses in the process of performing services for other City funds and receive reimbursement for direct, indirect, and overhead costs. Such instances include general government services and facilities maintenance services provided to other City funds. The Fiscal Year 2005 Proposed Budget projects Charges for Current Services at \$77.6 million, a 9.5 percent increase over the Annual Fiscal Year 2004 Budget. Refer to Schedule III of this Financial Summary for a breakdown of the budgetary data by subcategory.

Total City Budget
\$747.1 million

General Fund Budget
\$77.6 million

Percent of General Fund
9.5%

Other Revenue

Other Revenue represents 0.1 percent of total General Fund revenue and mainly consists of refunds and revenue generated from the sale of publications and excess inventory. However, this category represents a substantial portion of the revenue in other funds.

Total City Budget
\$259.0 million

General Fund Budget
\$0.9 million

Percent of General Fund
0.1%

Transfers from Other Funds

The revenue in the Transfers from Other Funds category reflects transfers to the General Fund from various other funds including a transfer from Special Promotional Programs to cover the costs of maintenance of tourist-oriented facilities.

Total City Budget
\$284.0 million

General Fund Budget
\$66.3 million

Percent of General Fund
8.1%